

WATER/TAC/LTR: jrb

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

WATER DIVISION

RESOLUTION NO. W-4421

September 4, 2003

R E S O L U T I O N

**(RES. W-4421), WATERTEK, INC., OAK HILLS DISTRICT (OH).
ORDER DENYING AUTHORIZATION OF RECOVERY OF
UNANTICIPATED EXPENSES AND ORDER AUTHORIZING A
RATE BASE OFFSET, PRODUCING ADDITIONAL REVENUES
OF \$795 OR 0.3%.**

SUMMARY

By Advice Letter No. 15, filed on April 2, 2003, OH requested revision of Schedule No. 2, Flat-Rate Service, to offset unanticipated emergency system repairs totaling \$50,123.25, or an increase in revenues of 23.3%. OH requests that a 12-month surcharge of \$9.20 per customer be utilized to recover the unanticipated expenses from its 454 customers.

Ordering Paragraph (O.P.) No. 2 of D. 92-03-093 authorized Class C and Class D **water** utilities to establish a memorandum account to track unanticipated costs of repairs necessary for a utility's service to its customers and to notify the Water Division by letter when it had done so. Since OH is a sewer utility, the memorandum account is not available to OH and this resolution denies recovery of unanticipated costs. The Commission does find that the expenditure of \$50,123.25 was reasonably spent on plant replacement and this investment should be classified as rate base.

BACKGROUND

Ordering Paragraph (O.P.) No. 2 of D. 92-03-093 authorized Class C and Class D water utilities to establish a memorandum account to track unanticipated costs of repairs necessary for a utility's service to its customers and to notify the Water Division by letter when it had done so. It also authorized the utilities to file by advice letter, or as part of a general rate case, to recover the costs recorded in the memorandum account either in rates or in a one-year surcharge when the total

cost exceeded 2% of the utility's last adopted gross revenues. Costs that were already reflected in rates or recoverable through insurance, or other means, and costs that with reasonable diligence could have been avoided would not be recoverable through the memorandum account.

Watertek provides water and sewer services to six CPUC-regulated entities (districts) and contracts for services to one additional water and sewer entity. The six CPUC-regulated districts are: East Plano (Porterville area water system), Grandview Gardens (Porterville area water system), Indian Springs (Salinas area sewer system), Metropolitan (Fresno area water system), Oak Hills (Salinas area sewer system), and Spreckles (Salinas area sewer system). The non-regulated sewer entity is San Lucas (Salinas area water and sewer system).

By letters dated September 8, 2001, Watertek, Inc. informed the Water Division that it had established Extraordinary Event Memorandum Accounts (EEMA) and Catastrophic Event Memorandum Accounts (CEMA) for all districts, both water and sewer.

The present rates of OH became effective on December 6, 2002, pursuant to Commission Resolution W-4354 which authorized a general rate increase of \$98,815, or 84.9%, and allowed a 20% return on margin. OH presently serves 454 flat-rate residential sewer customers located approximately three miles east of the city of Castroville, Monterey County.

DISCUSSION

The Commission, as of July 22, 2003, regulates approximately 12 sewer utilities. The Commission did not reference sewer utilities in D.92-03-093, when it authorized the establishment of memorandum accounts for unanticipated expenses. Although the EEMA and CEMA are valid for the water utilities under the ownership of Watertek, Inc., absent Commission authorization, they are not now valid for sewer utilities and therefore not for OH.

The Water Division has reviewed and verified OH's expenditures and determined that these expenditures should be classified as additions to rate base. The Water Division finds that these expenses were necessary and reasonable.

In D.92-03-093, effective April 30, 1992, the CPUC adopted the operating ratio method of ratemaking as an alternative to return on rate base method for Class C

and Class D utilities. Thus, two methods are available to Staff to utilize in calculating a reasonable profit: Return on Rate Base (not investment) and Operating Ratio. Staff first calculates the revenue requirement utilizing the rate of return method and then calculates the revenue requirement utilizing the operating ratio method. Policy dictates that Staff will recommend the method that produces the higher revenues.

In the operating ratio method, the utility's revenue requirement is defined as the sum of its operating and maintenance expenses, depreciation expenses, income and other taxes, and an operating margin. A 20% rate of margin has historically been used to determine the margin over and above operating, maintenance and depreciation expenses.

Comparison of the revenue requirement in OH's last general rate case indicated that the operating ratio method produced a higher revenue requirement than the return on rate base method. In keeping with policy, Staff recommended the operating ratio method for determining the revenue requirement.

Even though comparison with a rate base offset indicates that the operating ratio method continues to produce a higher revenue requirement adding this amount to plant results in increased depreciation expense and income tax. OH should adjust plant in service and depreciation reserve in order to reflect a correct amount of rate base. The increase for depreciation and income tax will not result in a rate of return greater than last authorized for OH.

Service is satisfactory. There are no Commission orders requiring system improvements and there are no service problems requiring corrective action. OH currently complies with all Commission orders and regulations.

The Consumer Affairs Branch has received one miscellaneous rate complaint against Watertek, Inc. from July 1, 2002 to July 1, 2003.

NOTICE AND PROTESTS

OH has given notice of the request by mailing it on April 18, 2003, to each of its customers. Eleven protests were received by the Water Division. All opposed the increase in light of the recently granted general rate case. Several protestors accused the owner of poor management practices and of not maintaining a sufficient maintenance and repair program.

The Water Division has taken all protests into consideration and has determined that the requested recovery through a rate base offset is proper. Nothing was presented in the protests that would support another conclusion.

FINDINGS

1. In May 2002, the Oak Hills District of Watertek, Inc. requested to recover the unanticipated emergency sewer pipeline repairs. Recovery of these expenses was requested, on a dollar-by-dollar basis, by a 12-month surcharge of \$9.20 per month from each of its 454 sewer customers in the Oak Hills District.
2. Eleven customers have protested the requested surcharge. All protests have been taken into consideration.
3. Decision 92-03-093 authorized Class C and Class D water utilities to establish a memorandum account to track unanticipated costs of repairs and to file for recovery when the total cost exceeded 2% of the utility's last adopted gross revenues.
4. On September 8, 2001, Watertek, Inc. informed the Water Division that it had established Extraordinary Event Memorandum Accounts and Catastrophic Event Memorandum Accounts for all districts, both water and sewer.
5. Decision 92-03-093 did not reference the applicability of memorandum accounts to sewer utilities, and therefore OH is not eligible to recover costs under the established Extraordinary Event Memorandum Accounts and Catastrophic Event Memorandum Accounts.
6. \$50,123.25 should be recorded in the Oak Hills District's utility plant account.
7. Comparison of the revenue requirement indicates that the operating ratio method produces a higher revenue requirement than the return on rate base method. In keeping with policy, Staff recommends the operating ratio method for determining the revenue requirement.
8. The Commission finds, after investigation by the Water Division, that the changes hereby authorized are justified and the resulting rates are just and reasonable.

THEREFORE IT IS ORDERED THAT:

1. Watertek Inc., Oak Hills District, shall file a supplemental advice letter to incorporate the revised rate Schedule No. 2, Flat Rate Service, attached to this resolution as Appendix A, and concurrently cancel its presently effective rate schedule. The effective date of the revised schedule shall be five days after the date of filing.
2. Watertek Inc. is authorized to record \$50,123.25 in its Oak Hills District's utility plant account.
3. This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed, and adopted at a conference of the Public Utilities Commission of the State of California held on September 4, 2003; the following Commissioners voting favorably thereon:

WILLIAM AHERN
Executive Director

MICHAEL R. PEEVEY
President
CARL W. WOOD
LORETTA M. LYNCH
GEOFFREY F. BROWN
SUSAN P. KENNEDY
Commissioners

APPENDIX A

Schedule No. 2

FLAT-RATE SERVICE

APPLICABILITY

Applicable to all flat-rate service.

TERRITORY

Subdivisions of Oak Hills and Indian Springs, and the community of Spreckels, in the vicinity of Salinas, Monterey County.

RATES

	<u>Per Quarter</u>		<u>Per Month</u>
	<u>Oak Hills</u>	<u>Spreckels</u>	<u>Indian Springs</u>
For each residential customers and small commercial service connection	\$120.00 (I)	\$107.00	\$49.54
For each service connection of a school		\$160.00	
For each service connection of a commercial establishment with 4 or more employees		\$214.00	
For each industrial service connection		\$641.00	

SPECIAL CONDITIONS

1. All bills are subject to the reimbursement fee set forth in Schedule No. UF.
2. Spreckels customers may remit quarterly bills in three equal installments on the first day of the month.